

carryover from a separate return limitation year at that time, the group does not treat any expiration of the loss carryover (even if in a tax year beginning on or after January 1, 1995) as a noncapital, nondeductible expense resulting in a negative adjustment under this section. If S becomes a member of a consolidated group in a consolidated return year beginning on or after January 1, 1995, and S has a loss carryover from a separate return limitation year at that time, adjustments with respect to the expiration are determined under this section.

(5) *Prior law*—(i) *In general*. For prior determinations, see prior regulations under section 1502 as in effect with respect to the determination. See, e.g., §§1.1502-32 and 1.1502-32T as contained in the 26 CFR part 1 edition revised as of April 1, 1994.

(ii) *Continuing basis reductions for certain deconsolidated subsidiaries*. If a subsidiary ceases to be a member of a group in a consolidated return year beginning before January 1, 1995, and its basis was subject to reduction under §1.1502-32T or §1.1502-32(g) as contained in the 26 CFR part 1 edition revised as of April 1, 1994, its basis remains subject to reduction under those principles. For example, if S ceased to be a member in 1990, and P's basis in any retained S stock was subject to a basis reduction account, the basis remains subject to reduction. Similarly, if an election could be made to apply §1.1502-32T instead of §1.1502-32(g), the election remains available. However, §§1.1502-32T and 1.1502-32(g) do not apply as a result of a subsidiary ceasing to be a member in tax years beginning on or after January 1, 1995.

(6) [Reserved]. For further guidance, see §1.1502-32T(h)(6).

[T.D. 8560, 59 FR 41685, Aug. 15, 1994, as amended by T.D. 8677, 61 FR 33323, June 27, 1996; T.D. 8560, 62 FR 12098, Mar. 14, 1997; T.D. 8823, 64 FR 36099, July 2, 1999; T.D. 8984, 67 FR 11040, Mar. 12, 2002; T.D. 9048, 68 FR 12291, Mar. 14, 2003]

§ 1.1502-32T Investment adjustments (temporary).

(a) and (a)(1) [Reserved]. For further guidance, see §1.1502-32(a) and (a)(1).

(a)(2) *Application of other rules of law*. The rules of this section are in addition

to other rules of law. See, e.g., section 358 (basis determinations for distributees), section 1016 (adjustments to basis), §1.1502-11(b) (limitations on the use of losses), §1.1502-19 (treatment of excess loss accounts), §1.1502-31 (basis after a group structure change), and §1.1502-35T (additional rules relating to stock loss, including losses attributable to worthlessness and certain dispositions not followed by a separate return year). P's basis in S's stock must not be adjusted under this section and other rules of law in a manner that has the effect of duplicating an adjustment. For example, if pursuant to §1.1502-35T(c)(3) and paragraph (b)(3)(iii)(C) of this section the basis in stock is reduced to take into account a loss suspended under §1.1502-35T(c)(1), such basis shall not be further reduced to take into account such loss, or a portion of such loss, if any, that is later allowed pursuant to §1.1502-35T(c)(5). See also paragraph (h)(5) of this section for basis reductions applicable to certain former subsidiaries.

(b) through (b)(3)(iii)(B) [Reserved]. For further guidance, see §1.1502-32(b) through (b)(3)(iii)(B).

(b)(3)(iii)(C) *Loss suspended under §1.1502-35T(c)*. Any loss suspended pursuant to §1.1502-35T(c) is treated as a noncapital, nondeductible expense incurred during the taxable year that includes the date of the disposition to which such section applies. See §1.1502-35T(c)(3). Consequently, the basis of a higher-tier member's stock of P is reduced by the suspended loss in the year it is suspended.

(D) *Loss disallowed under §1.1502-35T(g)(3)(iii)*. Any loss or deduction the use of which is disallowed pursuant to §1.1502-35T(g)(3)(iii) (other than a loss or deduction described in §1.1502-35T(g)(3)(i)(B)(II)), and with respect to which no waiver described in paragraph (b)(4) of this section is filed, is treated as a noncapital, nondeductible expense incurred during the taxable year that such loss would otherwise be absorbed. See §1.1502-35T(g)(3)(iv).

(b)(4) through (b)(4)(iv) [Reserved]. For further guidance, see §1.1502-32(b)(4) through (b)(4)(iv).

(b)(4)(v) *Special rule for loss carryovers of a subsidiary acquired in a transaction for which an election under §1.1502-*

20T(i)(2) is made—(A) Expired losses. Notwithstanding § 1.1502-32(b)(4)(iv), to the extent that S's loss carryovers are increased by reason of an election under § 1.1502-20T(i)(2) and such loss carryovers expire or would have been properly used to offset income in a taxable year for which the refund of an overpayment is prevented by any law or rule of law as of the date the group files its original return for the taxable year in which S receives the notification described in § 1.1502-20T(i)(3)(iv) and at all times thereafter, the group will be deemed to have made an election under § 1.1502-32(b)(4) to treat all of such expired loss carryovers as expiring for all Federal income tax purposes immediately before S became a member of the consolidated group.

(B) *Available losses.* Notwithstanding § 1.1502-32(b)(4)(iv), to the extent that S's loss carryovers are increased by reason of an election under § 1.1502-20T(i)(2) and such loss carryovers have not expired and would not have been properly used to offset income in a taxable year for which the refund of an overpayment is prevented by any law or rule of law as of the date the group files its original return for the taxable year in which S receives the notification described in § 1.1502-20T(i)(3)(iv) and at all times thereafter, the group may make an election under § 1.1502-32(b)(4) to treat all or a portion of such loss carryovers as expiring for all Federal income tax purposes immediately before S became a member of the consolidated group. Such election must be filed with the group's original return for the taxable year in which S receives the notification described in § 1.1502-20T(i)(3)(iv).

(C) *Effective date.* This paragraph (b)(4)(v) is applicable on and after March 7, 2002.

(b)(4)(vi) *Special rules in the case of certain transactions subject to § 1.1502-35T.* If a member of a consolidated group transfers stock of a subsidiary member and such stock has a basis that exceeds its value immediately before such transfer or a subsidiary member is deconsolidated and any stock of such subsidiary member owned by members of the group immediately before such deconsolidation has a basis that exceeds its value, all members of

the group are subject to the provisions of § 1.1502-35T(b), which generally require a redetermination of members' basis in all shares of subsidiary stock. In addition, if stock of a subsidiary member is treated as worthless under section 165 (taking into account the provisions of § 1.1502-80(c)), or if a member of a group disposes of subsidiary member stock and on the following day the subsidiary is not a member of the group and does not have a separate return year, and the common parent makes an election under § 1.1502-35T(f)(2) to reattribute to itself the losses treated as attributable to such subsidiary member, § 1.1502-35T(f)(2) requires a reduction of members' basis in shares of subsidiary stock.

(c) through (h)(5)(ii) [Reserved]. For further guidance, see § 1.1502-32(c) through (h)(5)(ii).

(h)(6) *Loss suspended under § 1.1502-35T(c) or disallowed under § 1.1502-35T(g)(3)(iii).* Paragraphs (a)(2), (b)(3)(iii)(C), (b)(3)(iii)(D) and (b)(4)(vi) of this section are effective on and after March 7, 2002, and expire on March 11, 2006.

[T.D. 9048, 68 FR 11291, Mar. 14, 2003; 68 FR 16431, Apr. 4, 2003]

§ 1.1502-33 Earnings and profits.

(a) *In general—(1) Purpose.* This section provides rules for adjusting the earnings and profits of a subsidiary (S) and any member (P) owning S's stock. These rules modify the determination of P's earnings and profits under applicable rules of law, including section 312, by adjusting P's earnings and profits to reflect S's earnings and profits for the period that S is a member of the consolidated group. The purpose for modifying the determination of earnings and profits is to treat P and S as a single entity by reflecting the earnings and profits of lower-tier members in the earnings and profits of higher-tier members and consolidating the group's earnings and profits in the common parent. References in this section to earnings and profits include deficits in earnings and profits.

(2) *Application of other rules of law.* The rules of this section are in addition to other rules of law. For example, the allowance for depreciation is determined in accordance with section